

**The Railroad Week in Review**  
**May 9, 2003**  
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**R**ailAmerica total sales in 1Q03 rose 1% to \$107.2 mm yoy while operating expenses increased 6% to \$86.3 mm. Operating income thus slid 18% to \$16 mm. However, to get apples-to-apples comps with the other roads, we have to add back the gain on asset sales taken to reduce expenses in both years. Transportation and GS&A expense remained relatively constant at \$61 mm and \$22 mm respectively. Depreciation was \$9 mm in 1Q03 and \$8 mm a year ago. Operating ratios if we stopped here would be 85.4 and 85.8 in 1Q03 and 1Q02 respectively.

Taking out the asset gains of \$0.4 mm this quarter and \$4.6 mm a year ago gives new full-railroad operating ratios of 85.1 and 81.6, a 3.5-point negative spread yoy. IMHO the former is the more accurate picture of how well RRA is doing at the core business. And it seems to me it's customary to post asset sales below the line between operating income and net income.

North American freight sales grew 5% to \$86.4 mm while expenses held the line at \$67 mm yielding a 4.1 point NA operating ratio improvement to a highly respectable 77.9. Commodity revenue and car-count figures indicate gains in coal, petroleum and "other" offset declines in low-rated commodity groups like bridge traffic and agricultural. So the news that overall NA freight sales were up on the same number of carloads is a positive.

Australian revenue decreased 13% to \$20.8 mm on 26% fewer carloads, so at least margins are holding. Moreover, Freight Australia has won two new, three-year transportation agreements valued at more than US\$13 mm and further diversify the railroad's grain-dominated commodity base. Ferronor results have been moved to discontinued operations, never mind the fact 1Q03 sales rose 16% yoy to \$6.2 mm primarily due to its new copper ore and natural gas contracts.

**KCS** purchasers of its initial \$175 million offering of Redeemable Cumulative Convertible Perpetual Preferred Stock have exercised their option to purchase an additional \$25 million of the preferred stock. The terms of the private offering were announced on April 30, 2003. KCS anticipated closing on the entire \$200 million transaction by the end of the day, May 5, 2003. The preferred stock, and the common stock to be issued on the conversion of the preferred stock, have not been registered under the Securities Act of 1933, as amended, and may not be offered or sold in the United States absent registration or an applicable exemption from registration requirements.

S&P gives a "B" rating to the Redeemable Cumulative Convertible Perpetual Preferred. Meanwhile, S&P also announced that KCS and The Kansas City Southern Railway Company (KCSR), including the "BB" corporate credit rating, remain on Credit Watch. Moody's Investor Services assigned its B3 rating to the KCS Redeemable Cumulative Convertible Perpetual Preferred Stock offering, and downgraded KCS senior implied and senior unsecured debt.

**N**orfolk Southern shareholders at this week's annual meeting narrowly defeated a proposal to end staggered terms for the railroad company's board members. About 51.4 percent of the company's shares were voted against the proposal to make the nine board members stand election every year. The proposal would have ended the current system under which three members stand election each year for three years.

The shareholder proposal was put forth, according to the proxy statement, in order to make all board members stand election each year would make the board more responsible to stockholders and “give the company the flexibility it needs as it moves into the future.” As one might expect, the NS board demurred, saying the current system “allows directors to have a long-term focus in the management of the business.” I knew it would be a close one when a week before the vote a telemarketer called to urge me to send in my proxy if not done already. That was a first.

**P**ennsylvania DOT Secretary Allen Biehler led off the 2003 Joint Rail Freight Seminar with a call for greater intermodal (no caps) cooperation and integrated distribution systems. He spoke specifically of the large amount of construction aggregates and long-distance boxes on Penna highways and urged participants to find ways to do more with rail. To which CP’s Paul Gilmore added, “Rail *can* do more, and shame on us if we don’t find the ways.”

Every May this program gets better. We heard from Dan Mazur of NS, Jim Howarth of CSX and GWR’s Dave Collins on “Strategic Opportunitites for Rail.” Collins said B&P customers have invested more than \$1 bn in their own rail-related infrastructure because they’re convinced “rail is here to stay.” Howarth ticked off new shortline opportunities with CSX, and Mazur wrapped by saying the new NS operating systems have so reduced standard deviations of service variability “there is no place to hide.”

Between formal presentations there was ample opportunity to see what the various participants were up to in their respective bailiwicks, and the news was universally encouraging. Penn DOT is running an internal training program to get everybody current on rail matters. There were new shortline customers shifting thousands of carloads to the rails from the highways. As GVT’s Chuck Riedmiller put it, “We don’t say ‘no’ to any customer.”

The only soft spots were 286-capacity and interchange process. With respect to the former, Penn DOT funds and the RRIF program are available to shortlines willing to run the numbers and make the business case. Getting fluid interchange requires the class 1s to be consistent in data management between and among shortlines. It requires a shortline commitment to total e-connectivity. And it requires both to “reduce the standard deviations of service variability.”

Next year’s Penna Rail Freight Seminar will be in State College May 5-7, 2004. Shipper participation was good this year, and still more would be even better. Here’s why. For more than a year one group has been trying to find put together a commodity lane involving two shortlines and a class 1. The conference put everybody in the same place and over coffee, cocktails and barbecue they came up with a process to explore the options in an orderly manner. And if that’s not a reason to descend on State College next May I don’t know what is.

**C**anadian National has locomotives for sale. Details are on the web at [www.cn.ca](http://www.cn.ca) under the “Sale of Surplus Asset” tab in the lower left corner. Most of the units are four-axle under 2000 horsepower, including a single set of F9 A and B units. Most were built in the late 1950s and early 1960s. The SD 40s and SD45s are a bit newer. Instructions to bidders, terms, loco locations and descriptions and even bid forms are all downloadable PDFs.

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